FILED
SEP 17 1953
HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1953.

No. 275.

PUBLIC COMMON STOCKHOLDERS' PROTECTIVE COMMITTEE OF ARKANSAS NATURAL GAS CORPORATION,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION, CITIES SERVICE COMPANY, ARKANSAS NATURAL GAS CORPORATION, ARKANSAS LOUISIANA GAS COMPANY, ARKANSAS FUEL OIL COMPANY, CLASS A COMMON STOCK COMMITTEE,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit.

BRIEF FOR RESPONDENT CITIES SERVICE COMPANY IN OPPOSITION.

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September, 1953.

Pandick Press, Inc., 22 Thames St., New York 6, N. Y., U. S. A.

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Opinions Below.

The opinion of the District Court (R. 5a) is reported at 109 F. Supp. 522. The opinion of the Court of Appeals (R. 66a) is reported at 204 F. 2d 797.

Jurisdiction.

The judgment of the Court of Appeals was entered on May 28, 1953 (R. 67a). The Petition for a Writ of Certiorari was filed on August 20, 1953. The jurisdiction of this Court is invoked under 28 U. S. C. 1254(1).

Questions Presented.

Where a plan of reorganization of a holding company approved under Section 11(e) of the Public Utility Holding Company Act of 1935 provides for ratable distribution of its assets among the stockholders and an additional payment by its majority stockholder out of its own assets directly to public holders of one class of stock in settlement of an alleged class claim or special equities of the latter against such majority stockholder, have the public holders of another class of stock standing to attack the approval of the plan on the sole ground that the class claim was invalid and the payment a windfall to the recipients, although a holding to that effect would not entitle the complaining stockholders to receive any more than they have already received under the plan?

Assuming *arguendo* an affirmative answer to the foregoing question, did the Commission have authority to approve a settlement of claims, including the settlement of said class claim, without adjudicating the contested issues of law and fact involved in the claims?

Statement of the Case.*

Arkansas Natural Gas Corporation (Arknat) was formed in 1928 by merger of a corporation controlled by Pittsburgh interests with properties owned by Cities

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* References (R.) refer to pages of the record; references (R. , p.) refer to the record page and the page or pages of a document of more than one page having only one record page number; references (R. 63a, Cit. App.) refer to pages of the Appendix to the Brief of Cities Service Company in the Court of Appeals, which appear between record pages 62a and 64a; references (Pet.) refer to the petition for writ of certiorari; and references (Br.) refer to the brief in support of the petition.

Service Company (Cities). By the terms of the merger agreement Cities received a substantial amount of Preferred Stock and 60% of the Common Stock, all of which it retained throughout (R. 62a, pp. 22, 23 and 43).

The new company embarked on a period of rapid expansion, which it financed in part through earnings and in part through the sale of a new Class A Stock, which was in all respects the same as Common Stock except that it did not have the right to vote (R. 5a, p. 2). The first block of Class A Stock was offered to the common stockholders and Cities took and paid for its proportion (R. 38a, 62a, p. 33). An additional 2,500,000 shares were marketed by Cities (through its wholly owned subsidiary) to the public and the net proceeds thereof were remitted to Arknat (R. 62a, pp. 33-34). In the process, Cities also increased its own stockholdings and on the effective date of the Plan owned about 75% (3,059,267 shares) of the Common Stock and about 25% (857,112 shares) of the Class A Stock (R. 62a, p. 3).

Arknat conducted its business substantially through two subsidiaries, Arkansas Louisiana Gas Company (Arkla) and Arkansas Fuel Oil Company (Arkfuel) (R. 62a, pp. 3, 53). Since the former was engaged in all phases of the natural gas business, including the distribution of gas at retail, it was a public utility company as defined by the Public Utility Holding Company Act of 1935 ("Act"). Arknat was therefore required to register as a holding company. Cities, by reason of this and other utility interests, was also required to register as a holding company.

In 1941 the Securities and Exchange Commission (Commission) began a proceeding under Section 11(b)(1) of the Act to determine what properties might be retained and what must be disposed of. A decision was rendered by the Commission in 1944 (In the Matter of Cities Service

Company and its Subsidiary Companies, 15 S. E. C. 962) which, so far as Arknat was concerned, in substance required it to dispose of either its utility business or its oil business (R. 62a, p. 4).

In 1949 the Commission commenced a proceeding under Section 11(b)(2) of the Act against both Cities and Arknat questioning the corporate structure and accounts of the latter, and setting forth many allegations concerning its past history. Both Cities and Arknat answered and later Arknat filed a plan intended to satisfy both the earlier order and the issues raised by the new proceeding (R. 62a, pp. 4-5). In substance the plan provided for merger of Arknat and Arkfuel, retirement of the Preferred Stock at the redemption price, and ratable distribution to Arknat's Class A and Common stockholders of the Common Stocks of the merged company and of Arkla (R. 62a, p. 5). This would effect a separation of the public utility business from the oil business in compliance with Section 11(b)(1), and would eliminate both the holding company and the non-voting stock in compliance with Section 11(b)(2) (R. 62a, p. 7). Lengthy hearings were thereafter held, largely devoted to a minute examination by the Commission's staff of all dealings between Cities and Arknat and primarily the marketing of the A Stock, with a view to showing that there were potential claims against Cities which should be taken cognizance of in the proceeding—these being issues raised by the order which commenced the proceeding.

These alleged claims were of two types. On the one hand there were transactions which it was alleged gave rise to ordinary corporate claims in favor of Arknat against Cities which, if established, would of course redound to the benefit of both the Common or Class A stockholders without distinction. On the other hand, it was charged that in the marketing of the Class A stock Cities had been

guilty of fraud, misrepresentation and breach of fiduciary duty to those stockholders; and as to this claim (sometimes called the "class claim") it was asserted—and later found by the Commission—that Arknat and its Common stockholders, far from being the victims, in fact shared in the benefits through the allegedly excessive prices obtained for the Class A stock from the public (R. 62a, pp. 19, 49).

After some 2,600 pages of testimony had been taken and more than 230 exhibits introduced at the hearings held intermittently over a period of eight months, Cities deemed it advisable to make an offer to settle the alleged claims against it and thereupon joined with Arknat in filing an amended plan (hereinafter called the "Plan") (R. 62a, p. 5). Its new feature was an offer by Cities to compromise all claims by payment of $1.50 per share to public holders of Class A Stock and 25¢ per share to public holders of Common Stock. The offer was intended and has been treated throughout by all parties as a payment to all of the stockholders of 25¢ per share in settlement of the corporate claims, and an additional payment to the holders of Class A Stock of $1.25 per share in settlement of the so-called class claim (R. 62a, pp. 50-51).

Hearings were resumed. The Class A Committee contended that each figure was inadequate, whereas the Common Stock Committee contended that the "corporate claim" figure was inadequate and all stockholders should be paid more on that account, but that there was no basis for different treatment of the two classes of stock because there was no valid class claim (R. 62a, p. 20). The Commission found that the settlement was fair and equitable and entered an order approving the Plan. The Commission then applied to the United States District Court for the District of Delaware for an order of enforcement, as pro-

vided in Section 11(e) of the Act. The two committees again urged their objections to the settlement, but Maris, J. (sitting by special designation) likewise found that the Plan, including the settlement of claims, was fair and equitable and entered an enforcement order (R. 5a-11a).

In the Court of Appeals, the present Petitioners were the sole appellants, and their appeal was limited to that part of the Plan which provided for the settlement of the class claim or special equities of the holders of Class A Stock. The Court of Appeals affirmed the order of the District Court, stating that Petitioners were not aggrieved by and had no standing to complain of the part of the settlement appealed from, and also that it was satisfied with the review of the merits of the Plan by the District Court (R. 68a).

The enforcement order required that the Plan be consummated unless a stay was granted. Since no stay was obtained, Arknat and Cities consummated the Plan, including the claims settlement (R. 70a). On April 8, 1953, Cities sent to the Arknat stockholders checks in the amounts provided in the Plan to meet the terms of the settlement, of which nearly 99% of the approximately $4,000,000 thus payable have been cashed.

ARGUMENT.

Summary of Argument.

The questions which Petitioners seek to have this Court consider are not actually involved in the case. The actual issues below were neither novel nor difficult. The unanimous decisions below were in accordance with well-settled principles and manifestly just. The courts below properly held that Petitioners have no standing to complain in any event.

POINT I.

The Court below was correct in holding that Petitioners have no standing to attack the provision of the Plan for the settlement by Cities of the alleged class claim of the Class A stockholders because the holders of the Common Stock are not affected or aggrieved thereby.

The Commission found and concluded that the proposed payment by Cities of 25¢ per share to both the A Stock and the Common Stock in settlement of all corporate or derivative claims was fair and reasonable and approved the settlement (R. 62a, p. 50), and the District Court held that the Commission's findings and conclusions were supported by substantial evidence and were in accordance with law (R. 5a, p. 7). The Petitioners did not appeal to the Court of Appeals from this holding (Pet. 4) and expressly disaffirm any intention of asking this Court to review this holding (Br. 10).

Petitioners do not contend that they have any rights or claims against Cities other than their interest as stockholders of Arknat in the so-called corporate or derivative claims and, recognizing that they are bound as a matter of law by the holding above-mentioned, Petitioners are making no direct attack on the fairness of the settlement of the corporate claims. Their only contention is that the A Stock should not have been paid anything in settlement of the class claim.

This immediately raises the question of how the Petitioners can have a legitimate concern with the wholly separate settlement between Cities on the one hand and the Class A stockholders on the other hand. The payment of the additional amount by Cities to the A Stock in no way

decreased or affected the amount payable to the Common Stock. If, as Petitioners contend, such payment should not have been made because the class claim had no valid legal basis, a holding to that effect would merely entitle Cities to attempt to recover from the nearly 20,000 holders of A Stock the sums paid to them in settlement of such claim; it could not entitle the holders of Common Stock to receive more than the 25 cents per share already paid to them in settlement of the corporate claims. Cities, as the proponent of the settlement, is, of course, not complaining. It follows that the Common Stock is not injured or aggrieved by the settlement with the A Stock and the Court of Appeals properly so held.

Faced with this inescapable conclusion, Petitioners advance a number of arguments in an attempt to establish that the holders of the Common Stock are aggrieved:

(1) Petitioners assert (Br. 10-11) that the settlement violates the legal principle that stockholders with the same contract rights are entitled to ratable distribution of the assets of the enterprise. This principle was in no way violated here. The ordinary assets of the enterprise consisted of the stocks of the two subsidiaries and these have been distributed ratably. The other asset of the enterprise —the corporate claims—has likewise been distributed ratably through the payment to each stockholder of the identical amount per share in settlement thereof. The additional payment to the A Stock in settlement of their class claim was made by Cities out of its own assets. Since such payment in no way diminished the assets of the enterprise or the interest of the Common Stock therein, the doctrine appealed to has no application.

(2) Petitioners assert (Br. 11, *et seq.*) that if Cities and the Commission had understood the invalid character

of the class claim, Cities, nevertheless, might have offered the same aggregate amount in settlement to be applied solely to the corporate claims, and that the Commission would have approved such a settlement as fair and equitable both to Cities and to the stockholders of Arknat. This suggestion does violence both to the business judgment of Cities and the integrity of the Commission. The validity or invalidity of the class claim was completely irrelevant to the merit or lack of merit of the corporate claims. The fairness of the settlement of each was separately considered and determined on the basis of its own merits (R. 62a, pp. 19-51). Having urged no objection on appeal to the settlement of the corporate claims, the Common Stock Committee certainly has no standing to ask for a remand on the irresponsible suggestion that the Commission's findings and conclusions with respect to those claims may have been improperly influenced by its findings and conclusions with respect to the class claim.

(3) Petitioners assert that in fact Cities offered a total sum in settlement of all claims against it; that "it was the Commission and not Cities or ArkNat which made the allocation" (Br. 23); that the allocation of 25¢ per share to the Common and $1.50 per share to the A Stock was made by the Commission "as a prize court to divide up the booty" (Br. 17) and not by Cities; and that the Commission arbitrarily diverted "substantially all of the payment made by Cities to the Class A stockholders" (Br. 23), using the so-called class claim merely as a convenient excuse for that purpose.

This fanciful description is, of course, directly contrary to the facts. The first mention of settlement was in the Amended Plan filed by Cities and Arknat which contained the offer as mentioned above. This offer already contained

the full terms of the proposed settlement of the respective claims. It left nothing for the Commission to allocate and the proceedings before the Commission thereafter were directed solely to the question as to whether the offer was fair and equitable. Both the Commission and the District Court, in their consideration of the fairness of the settlement, treated the offer for what it was, to wit: a unilateral offer by Cities to compromise alleged claims asserted against it (R. 62a, p. 5; R. 5a, p. 4).

Petitioners (Br. 23-25) claim to find support for their version in the fact that certain officers of Cities or Arknat testified that they had no part in the preparation of the offer of settlement or were concerned only with the aggregate amount that Cities would be required to pay. The actual situation was clearly stated by Mr. Jones, President of Cities, who testified (R. 63a, Cit. App. 3a):

> "Q. Mr. Jones, did you make the determination that the $1.50 would be paid directly to Class A stockholders and 25¢ directly to the Common stockholders? A. No, I did not. I relied upon the legal counsel to consider the merits of these various claims and they did that job themselves.
>
> Q. Neither you nor anyone else in your Company made that suggestion? A. No, sir. The recommendation was made—I approved it when it was made but I did not have anything to do with the determination of it because I do not feel that I was in a position to pass on the merits of these legal questions that were raised."

Petitioners appear to nurse a sense of injury that it was counsel rather than the client who formulated the settlement offer. While we are unable to see any possible relevance, we suggest that in practically all cases involving complicated legal and factual issues, counsel is relied upon

for judgment as to the desirability and character of settlement. That Cities' officers were aware of the nature and potential seriousness of the Class A claim is shown by the testimony of Mr. Christian, Cities' Secretary and one of the principal witnesses (R. 63a, Cit. App. 2a).

The only other basis referred to by Petitioners for their version of the facts are assertions (Pet. 2) that "before the Commission, Cities resisted this discrimination between the two classes of stockholders and asserted that both classes should be afforded identical rights in accordance with the charter provisions" and "Thereafter, before the District Court, Cities accepted the Commission's decision and joined with it in asking enforcement of the Plan, * * *". And again (Pet. 4) "Cities from the beginning resisted any such allocation * * *."

These and similar statements by Petitioners are entirely disingenuous and give a completely false impression.

The simple facts are that until the settlement offer was made, Cities resisted all claims asserted against it, and argued that Arknat's assets should be distributed ratably to all stockholders including Cities. After it made the offer, Cities of course did its best to get the offer approved; it did not object to the differentiation in treatment of the two classes and it would, in fact, have been absurd for it to raise such objection to its own offer.

The sources referred to by Petitioners in support of their version of Cities' position are a quotation from Cities' brief before the Commission and supposed admissions in oral arguments in the Courts (Br. 25). Petitioners' confusion arises from their failure to recognize that Cities, in supporting the adequacy of its offer of settlement, was required to set forth the defenses which it would urge in the event of final adjudication on the merits. This Cities

did with respect to all the claims asserted—both corporate and class. The passage quoted by Petitioners from Cities' brief was part of such statement of defenses. We did not think that our purpose could be misunderstood, for that brief concluded with the following statement (R. 63a, Cit. App. 4a):

> "We feel confident that consideration of the nature of the claims and of the defenses thereto will lead to the conclusion that the terms of the compromise are generous to the holders of the A and Common Stock and represent an acceptable basis of disposing of these claims and thus terminating this lengthy reorganization proceeding and enabling the properties to resume the successful prosecution of their respective businesses without the uncertainties and difficulties arising from further litigation regarding these matters."

It is clear, therefore, that Petitioners are not aggrieved and have no standing to seek review in this Court.

POINT II.

Assuming *arguendo* that Petitioners be permitted to attack the compromise settlement of the special equities or class claim of the A Stock, the considerations upon which the Commission based its approval of such compromise, affirmed by the Courts below, were in accordance with established and uniform practice and precedents, and present no issue warranting review by this Court.

The Petitioners contend that the only remedy of the A Stock for the activities of Cities in marketing the A Stock lies in suits against Cities for damages or rescission by purchasers of such stock who claim to have been deceived

by the alleged fraud; that such claims do not pass to subsequent transferees of the stock by mere sale of the stock and assignment of the certificates; and that there is no such thing as a class claim of the A Stock which can be recognized in this proceeding.

As previously stated, Cities urged these same contentions in resisting these claims and later relied on them in support of the adequacy of its settlement offer. But neither principle, precedent nor sound administrative practice required it to conduct war to the uttermost. Despite its contentions, Cities was obliged to consider the costs and risks of litigating these issues to a final conclusion, including the risks of injury by delay to the enterprise itself (of which Cities owns the major portion). In making the offer of settlement Cities did not change its position but, as in all such offers, proposed an alternative to ultimate adjudication. This is equally true of both the corporate claims and the class claim of the A Stock. Petitioners inconsistently concede the propriety of settling the corporate claims without adjudication, but insist that a final adjudication of the class claim would be in favor of Cities and that therefore it is not a proper subject of settlement.

As we read the Commission's findings, it did not undertake to adjudicate the issues raised by any of the claims. It specifically repudiated such an approach—"In considering the claims asserted against Cities, 'we are not called upon to adjudicate the merits of or to assign a specific monetary value to each particular claim.' " (R. 62a, p. 42.) Recalling particularly that both aspects of the settlement were under attack as inadequate, the Commission carefully reviewed each claim and the defenses thereto and then indicated what elements of the claims including the Class A claim had in its opinion "sufficient merit to require recognition" (R. 62a, p. 42) in a settlement proposal, and con-

cluded that the proposal was adequate as a compromise of all claims worthy of consideration (R. 62a, p. 50).

This has been the invariable practice of the Commission in dealing with proposals to settle alleged claims, and it has been repeatedly approved by the Courts. As stated in *In re North American Light & Power Co.*, 170 F. 2d 924, (C. A. 3, 1948), at page 933:

> "It would be anomalous, indeed, were the Commission to have on the one hand authority to approve a settlement, and be required, on the other hand, to go through the motion of adjudicating the very subject of the settlement. We are here in agreement with the observations of the Court in *Ladd* v. *Brickley, supra,* at page 221 of 158 F. 2d;
>
> 'What was before the Court? It was not the decision upon the facts or law involved in the two lawsuits. * * * It was the determination of whether or not in view of all the issues involved in those cases the settlement was for the best interests of the estate being administered under its direction.' "

See also the authorities cited by the District Court below (R. 5a, p. 4).

The cases cited by the Petitioners (Br. 17-18) for the proposition that the courts will review the Commission's determinations of legal issues and will reverse them if erroneous, are not in point because in those cases there was no compromise settlement of disputed issues but decisions by the Commission based on erroneous determinations of settled judicial doctrines.*

The Commission was therefore following well established precedent in considering and approving the settle-

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* It is therefore unnecessary to consider whether these cases have been limited or modified by the second *Chenery* case, *Securities & Exchange Commission* v. *Chenery Corporation,* 332 U. S. 194.

ment of the asserted claims rather than requiring final adjudication of their validity. The District Court was clearly correct in holding that "the findings and conclusions of the Commission are supported by substantial evidence and are in accordance with law" (R. 5a, p. 7); and the Court of Appeals was properly "satisfied * * * with the review of the merits of the plan in the district court * * *" in addition to being "clear in its own collective mind that this appellant has no standing to complain of it in any event." (R. 68a). We submit that these rulings do not warrant further review.

Conclusion.

The petition is entirely without merit and should be denied.

Respectfully submitted,

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Dated September, 1953.